November 07, 2023

Poondiankuppam-Sattanathapuram Section Private Limited: Rating reaffirmed; outlook revised to Positive

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term loan	985.47	985.47	[ICRA]A reaffirmed and outlook revised to 'Positive' from 'Stable'
Total	**985.47**	**985.47**	

**Instrument details are provided in Annexure-I*

Rationale

The revised outlook for the reaffirmed rating of Poondiankuppam-Sattanathapuram Section Private Limited (PSSPL) factors in the alleviation of project execution risk in the backdrop of the advanced stage of project progress (~79% as of September 30, 2023), as reflected by the receipts of eight milestone payments from the National Highways Authority of India (NHAI). The rating favourably factors in the inherent benefits of the project's hybrid annuity-based nature, including upfront availability of right of way[1], de-scoping of right of way (RoW) pending beyond 180 days from the appointed date, inflation-linked[2] revisions to bid for project cost during the construction period and a relatively moderate funding risk. The risk is considered moderate, as 40% of the bid project cost (BPC) is to be funded by the NHAI during the construction period, in the form of grants and debt tie-up in place. The rating positively considers the credit support provided by the structural features of the debt, including the presence of escrow, a cash flow waterfall mechanism, provision for the creation of reserves and a restricted payment clause with a minimum DSCR of 1.15 times. The provision for reserves includes a debt service reserve account (DSRA) equivalent to six months' principal and interest (25% to be created on or before commercial operations date (COD) and the remaining to be created out of the first two annuities), a major maintenance reserve (MMR) and reserves to meet regular operations and maintenance (O&M) and interest obligations until the next scheduled annuity. The rating notes the stable revenue stream that is expected following the commissioning of the project with 60% of the inflation-adjusted BPC is paid out as annuity by the NHAI. Additionally, the NHAI [NHAI, rated [ICRA]AAA(Stable)], which is a strong counterparty, is also expected to cover the interest at an average of one-year MCLR of the top five scheduled commercial banks + 1.25% and the inflation-adjusted O&M cost bid over the 15-year operations period. PSSPL is also a subsidiary of Oriental Structural Engineers Private Limited (OSEPL), which has a long experience in the road construction segment and has been executing road projects since 1971. OSEPL has provided an undertaking for cost overrun during the construction phase.

The rating continues to derive comfort from the favourable financial profile and operational track record of its promoter, OSEPL. Further, OSEPL has provided an undertaking for the cost overrun during the construction phase, supporting any shortfall in O&M expenses and a corporate guarantee to meet the shortfall in the event of termination.

The rating is, however, constrained by the residual execution risks, including time and cost overruns. Nevertheless, the risk is mitigated to an extent by the fixed-price and fixed-time nature of the engineering, procurement, and construction (EPC) contractor and the strong project execution capabilities of its sponsor, OSEPL (rated [ICRA]AA (Stable)/[ICRA]A1+). ICRA takes note of the asset concentration risk owing to the dependency on a single project stretch for annuity receipt. The balance cost

[1] *At least 80% prior to the appointed date*

[2] *Based on annual change in price index multiple (PMI) from the base year – PMI is the weighted average of wholesale price index (WPI) and consumer price index (CPI) (IW) in the ratio of 70:30*

of ~Rs. 426.0 crore is expected to be funded by undrawn debt and authority grants, and the completion of the balance works by January 2024 remains a key rating monitorable. Further, the promoters have already infused nearly 90% of the equity requirement of Rs. 246 crore, as of September 2023, largely mitigating the funding risk. Once the project has been commissioned, the company will have to undertake O&M of the project stretch, as per the concession agreement to avoid any deduction from annuities. Any significant deduction from annuities or increase in routine and major maintenance (MM) from the budgeted level could impact its debt servicing coverage ratio. PSSPL's cash flows are exposed to inflation risks as O&M receipts, even though linked to the inflation index (70% WPI and 30% CPI), may not be adequate to compensate for the actual increase in O&M/periodic maintenance expenses.

The Positive outlook on the rating reflects ICRA's opinion that PSSPL's credit profile will improve over the near term with the expected receipt of PCOD upon completion of balance works and finalisation of project completion cost.

Key rating drivers and their description

Credit strengths

Established track record and strong financial profile of the sponsor and EPC contractor – PSSPL is a subsidiary of OSEPL, which has a long experience in the road construction segment and has been executing road projects since 1971. OSEPL has provided an undertaking for cost overrun during the construction phase, any shortfall in O&M expenses and corporate guarantee to meet the shortfall in the event of termination. OSEPL has a strong financial profile, which is supported by a regular stream of distribution from Oriental InfraTrust (rated [ICRA]AAA, OSEPL and its subsidiary Oriental Tollway Pvt Ltd cumulatively hold a 60% stake in Oriental InfraTrust).

Lower inherent risks in hybrid annuity mode (HAM) projects from the NHAI – The inherent benefits of the hybrid annuity-based nature of the project include an upfront availability of RoW, automatic de-scoping of RoW pending beyond 180 days from the appointed date and inflation-linked revisions to bid for project cost during the construction period. As of September 2023, the company already had RoW available for ~95% of the requisite land. Moreover, it faces a relatively lower equity mobilisation risk with 40% of the BPC to be funded by the authority, NHAI during the construction period in the form of a grant. A stable revenue stream, following the commissioning of the project, with 60% of the inflation-adjusted BPC will be paid out as annuity, along with interest at an average of one-year MCLR of the top five scheduled commercial banks + 1.25% and the inflation-adjusted O&M cost bid over the 15-year operations period by the NHAI. Such factors provide comfort and indicate lower inherent risks.

Healthy coverage indicators and presence of structural features – Once operational, PSSPL is expected to have a healthy debt service coverage ratio during the debt tenure. Structural features of the debt, such as the presence of escrow, a cash flow waterfall mechanism, provisions for DSRA (25% of the principal and interest for six months to be created on or before COD and the remaining to be created out of the first two annuities) and creation of MMR provide comfort. In addition, the presence of reserves to meet regular O&M and interest obligations until the next scheduled annuity, cash sweep and restricted payment clause with a minimum DSCR of 1.15 times, also mitigate the risk.

Credit challenges

Exposed to residual execution risks – The appointed date for the project was received on January 20, 2022, and as of September 2023, nearly 79% of the project has been completed. Thus, the company is exposed to residual project execution risks and completion of the work within the budgeted costs and timelines. However, the risk is mitigated to an extent by the fixed-price and fixed-time contract, and strong project execution capabilities of its sponsor/EPC contractor, OSEPL. The total estimated project cost of Rs. 2,080 crore is planned to be funded by the NHAI's grant of Rs. 848.2 crore, external debt (term loans) of Rs. 985.5 crore and equity/promoter contribution of Rs. 246.4 crore. Further, the promoters have already infused nearly 90% of the equity requirement of Rs. 246 crore as of September 2023, which largely mitigate the funding risk. The balance cost of ~Rs. 426.0 crore is expected to be funded by undrawn debt and authority grants.

Undertaking O&M as per concession requirement, cash flows and returns exposed to inflation risks – Following the commissioning of the project, the company will have to undertake the O&M of the project stretch, as per the concession agreement to avoid any deductions from annuities. Any significant deduction from annuities or increase in routine and MM from the budgeted level could impact its debt servicing coverage ratio. PSSPL's cash flows are exposed to inflation risks as the O&M receipts, even though linked to inflation (70% WPI and 30% CPI), may not be adequate to compensate for the increase in the O&M/periodic maintenance expenses. Hence, undertaking O&M within the budgeted costs will be a key rating sensitivity during the operations stage.

Liquidity position: Adequate

PSSPL's liquidity position is adequate. The pending cost of Rs. ~426.0 crore as on September 30, 2023, is expected to be funded by undrawn debt of Rs. 449.4 crore, the NHAI's remaining two grant payments and the balance through promoter's contribution. Further, the O&M expenses and interest servicing for the first six months following the COD will be funded as a part of the project cost.

Rating sensitivities

Positive factors – The rating could be upgraded if the project achieves PCOD/COD without any time and cost overruns.

Negative factors – Pressure on the rating could arise if there are any significant time and cost overruns, any additional indebtedness, or a material deterioration in the credit profile of the sponsor. The rating could come under pressure if there is any non-adherence or dilution of the debt structure.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for ROADS-HYBRID ANNUITY
Parent/Group support	Not Applicable
Consolidation/Standalone	Standalone

About the company

Poondiankuppam Sattanathapuram Section Private Limited (PSSPL) is a special purpose vehicle (SPV) promoted by Oriental Structural Engineers Private Limited (OSEPL) to undertake the four-laning of the existing road on the Poondiankuppam to Sattanathapuram (design Ch km 67.000 to km 123.800) section of NH 45A (new NH-332) in the state of Tamil Nadu under the NHDP Phase IV on design, build, operate and transfer (DBOT Annuity)/hybrid annuity model. As per the concession agreement (CA) signed between the NHAI and PSSPL on May 18, 2021, the concession period is 17 years (including a construction period of 730 days) from the appointed date (January 20, 2022).

Key financial indicators

Key financial indicators are not applicable as PSSPL is a project-stage company.

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as of Sep 30, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
					Nov 07, 2023	Dec 02, 2022	Dec 27, 2021	-
1	Fund-based facility – Term loan	Long term	985.47	535.84	[ICRA]A (Positive)	[ICRA]A (Stable)	[ICRA]A (Stable)	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund-based facility – Term loan	Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA’s website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Fund-based facility – Term loan**	November 2021	NA	*	985.47	**[ICRA]A (Positive)**

*Source: Company; * Linked with the COD of the project, estimated in August 2038*

[*Please click here to view details of lender-wise facilities rated by ICRA*]

Annexure II: List of entities considered for consolidated analysis – Not Applicable

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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